



Testimony

Before the Committee on Commerce, Science and
Transportation, U.S. Senate

For Release on Delivery
Expected at
9:30 a.m. EST
Thursday
February 1, 2001

AIRLINE COMPETITION

Issues Raised by Consolidation Proposals

Statement of JayEtta Hecker

Director, Physical Infrastructure Issues



G A O

Accountability * Integrity * Reliability

Form SF298 Citation Data

Report Date <i>("DD MON YYYY")</i> 01022001	Report Type N/A	Dates Covered (from... to) <i>("DD MON YYYY")</i>
Title and Subtitle AIRLINE COMPETITION Issues Raised by Consolidation Proposals		Contract or Grant Number
		Program Element Number
Authors JayEtta Hecker		Project Number
		Task Number
		Work Unit Number
Performing Organization Name(s) and Address(es) General Accounting Office, Washington, DC 20013		Performing Organization Number(s) GAO-01-370T
Sponsoring/Monitoring Agency Name(s) and Address(es)		Monitoring Agency Acronym
		Monitoring Agency Report Number(s)
Distribution/Availability Statement Approved for public release, distribution unlimited		
Supplementary Notes		
Abstract <p> We appreciate the opportunity to testify on the potential implications of merger proposals recently announced by major airlines. In May 2000, United Airlines (United) proposed to acquire US Airways and divest part of those assets to create a new airline to be called DC Air. More recently, American Airlines (American) has proposed to purchase Trans World Airlines (TWA), along with certain assets from United. These proposals have raised questions about how such consolidation within the airline industry could affect competition in general and consumers in particular. Extensive research and the experience of millions of Americans underscore the benefits that have flowed to most consumers from the 1978 deregulation of the airline industry, including dramatic reductions in fares and expansion of service. These benefits are largely attributable to increased competition--by the entry of both new airlines into the industry and established airlines into new markets. At the same time, however, airline deregulation has not benefited everyone; some communities have suffered from relatively high airfares and a loss of service due in part to a lack of competition. GAO has been analyzing aviation competition issues since enactment of the Airline Deregulation Act. Our work over the last decade has focused on challenges to competition and industry performance, including various mergers, the Department of Transportations (DOT) role, concentration in select airports, key airline operating and marketing practices, barriers to entry, small community service, and fares in dominated markets. 1 </p>		
Subject Terms		

Document Classification unclassified	Classification of SF298 unclassified
Classification of Abstract unclassified	Limitation of Abstract unlimited
Number of Pages 20	

Mr. Chairman and Members of the Committee:

We appreciate the opportunity to testify on the potential implications of merger proposals recently announced by major airlines. In May 2000, United Airlines (United) proposed to acquire US Airways and divest part of those assets to create a new airline to be called DC Air. More recently, American Airlines (American) has proposed to purchase Trans World Airlines (TWA), along with certain assets from United. These proposals have raised questions about how such consolidation within the airline industry could affect competition in general and consumers in particular.

Extensive research and the experience of millions of Americans underscore the benefits that have flowed to most consumers from the 1978 deregulation of the airline industry, including dramatic reductions in fares and expansion of service. These benefits are largely attributable to increased competition—by the entry of both new airlines into the industry and established airlines into new markets. At the same time, however, airline deregulation has not benefited everyone; some communities have suffered from relatively high airfares and a loss of service due in part to a lack of competition. GAO has been analyzing aviation competition issues since enactment of the Airline Deregulation Act. Our work over the last decade has focused on challenges to competition and industry performance, including various mergers, the Department of Transportation's (DOT) role, concentration in select airports, key airline operating and marketing practices, barriers to entry, small community service, and fares in dominated markets.¹

The potential shifts in industry structure that would be brought about from the proposed mergers represent a crossroads for the structure of the airline industry and the state of competition and industry performance.² These proposed mergers raise numerous public policy issues that require reasoned responses. Ultimately, the Department of Justice (DOJ) has the primary responsibility to evaluate these mergers. In its review, Justice considers a number of factors, including increases in market concentration; potential adverse effects on competition; the likelihood of new entry; possible efficiencies or other benefits; whether one of the airlines would fail and exit the market if the merger failed to occur; and whether a less anticompetitive alternative exists.

¹ See list of related GAO products attached to this statement.

² Technically, American has proposed to acquire the assets of TWA, which declared bankruptcy. For presentation purposes in this statement, however, we will refer to the transaction as a merger.

We recently issued a report on the potential effects of the proposed merger between United and US Airways.³ That review, using the most recently available data from DOT on the top 5,000 domestic airline markets, generally focused on changes in market structures and not on other issues that DOJ might take in consideration.⁴ Our statement today is based on that report and our earlier work on airline competition issues, along with initial analyses of the potential effects of the various proposed transactions between American, TWA, United, and US Airways. We will: (1) present an overview of potential shifts in industry structure and markets associated with both the American and United proposals; (2) identify key issues associated with American's proposed transactions; and (3) identify some critical public policy issues associated with the potential consolidation in the industry.

In summary:

- If both the United-US Airways merger and American-TWA acquisition are consummated, new United would have the largest market share of any U.S. carrier—over 27 percent—and new American would have a 22.6 percent share. Each proposal could have both harmful and beneficial effects on consumers. The United and American proposals would each reduce competition in approximately 300 markets, with each affecting over 10 million passengers. Each proposal would allow the new larger carrier to dominate (i.e., obtain a greater than 50-percent market share) more than 100 new markets. However, the mergers would also each create new competitors where, previously, each of the merging carriers had less than a 10-percent market share. Each would provide other benefits to consumers as well, such as creating new online service in certain markets and possible new routings allowing passengers to connect over different cities.

³ *Aviation Competition: Issues Related to the Proposed United Airlines—US Airways Merger* (GAO-01-212, Dec. 15, 2000).

⁴ We analyzed the most recent data available from DOT on the top 5,000 city-pair markets, which covered calendar year 1999. For this statement, we applied the same methodology, using the same data, as we did in our December 2000 report on the proposed United-US Airways merger. We recognize that competition or service in particular markets is likely to change over time with the entry or exit of different carriers. Carriers may add or reduce service in markets. These data illustrate the approximate orders of magnitude of the various transactions. We have not subtracted passengers or markets that may be affected by DC Air markets or the proposed agreement between United and American to share the current US Airways shuttle from the data for new United.

- American's proposed arrangements with TWA, United, US Airways, and DC Air raise a number of significant questions that cannot be answered now, in part because many of the details of these arrangements are still unknown. Although TWA has been in poor financial condition for years, the question remains whether American's purchase of TWA represents the least anticompetitive means to preserve its assets. Other questions arise about how the agreements that American has tentatively made with United (regarding the future of the US Airways Shuttle between Washington, New York, and Boston and the assets associated with the proposed DC Air) would affect competition.
- The consolidation in the industry that might result from both the proposed American and United transactions raises major public policy issues. These include, but are not limited to, questions about how a more consolidated industry might further raise barriers to market entry by new airlines, how the two merged airlines might compete in key markets, whether the merged carriers would expose the public to greater risks of travel disruptions, and how service to small communities might be affected.

Background

On May 24, 2000, United and US Airways agreed to merge their operations. Under the terms of the proposed merger, United would acquire US Airways in a transaction valued at \$11.6 billion. Specifically, United would pay \$60 for each share of common US Airways stock for a total of \$4.3 billion and would assume \$1.5 billion in US Airways net debt and \$5.8 billion in aircraft operating leases. According to information from United, the combined company ("new United") would have approximately 145,000 employees. It would operate eight hubs in six states and serve a total of 380 airports throughout the country, reaching communities in every state.

Under the terms of the proposed merger, United plans to divest some of the assets US Airways possesses at Ronald Reagan Washington National Airport (Reagan National). These assets would be used to create a new airline known as DC Air. They include 222 departure and arrival slots,⁵ several gates and related airport facilities, and the operations of an existing commuter airline.

⁵ The Federal Aviation Administration limits the number of operations (takeoffs and landings) that can occur during certain periods of the day at four congested airports—O'Hare in Chicago; Reagan National in

In January 2001, American proposed acquiring TWA (which declared bankruptcy) for approximately \$3.5 billion, including \$500 million in cash, \$3.0 billion in estimated lease assumptions, and \$200 million in other financing. In addition, American also announced that it had agreed with United to purchase certain assets from United and US Airways, including half of the US Airways Shuttle between Washington, New York, and Boston, and a 49-percent share of DC Air. According to information from American, the combined company (“new American”) would have approximately 120,000 employees. It would operate five hubs, nearly 1,000 aircraft, and gain a large number of slot and gate resources at key airports in the eastern United States.

The consummation of the proposed mergers is subject to approvals by various regulatory bodies. Both DOJ and DOT have responsibilities for reviewing airline mergers and acquisitions.⁶ DOJ has the authority to review mergers or stock acquisitions before they take place to determine whether they violate antitrust laws. Under the Hart-Scott-Rodino Act, an acquisition of voting securities above a set monetary amount must be reported to DOJ for prior review. DOJ has the authority to institute judicial proceedings under the Clayton Act if it determines that a merger or acquisition may substantially lessen competition in a relevant market or if it tends to create a monopoly.⁷ If DOJ believes any agreement is anticompetitive in whole or in part, it may seek to block the agreement in federal court. TWA’s bankruptcy proceeding is now before the U.S. Bankruptcy Court for the District of Delaware. DOT conducts its own analysis of airline mergers and acquisitions and submits its views and any relevant information in its possession to DOJ. In addition, when transactions involve the transfer of international route authority, DOT is responsible for approving such matters to ensure that they are consistent with the public interest.

Washington, D.C.; and Kennedy and LaGuardia in New York. The authority to conduct a single operation during these periods at these four airports is commonly referred to as a “slot.”

⁶ The merger may also be reviewed by the European Commission and state attorneys general.

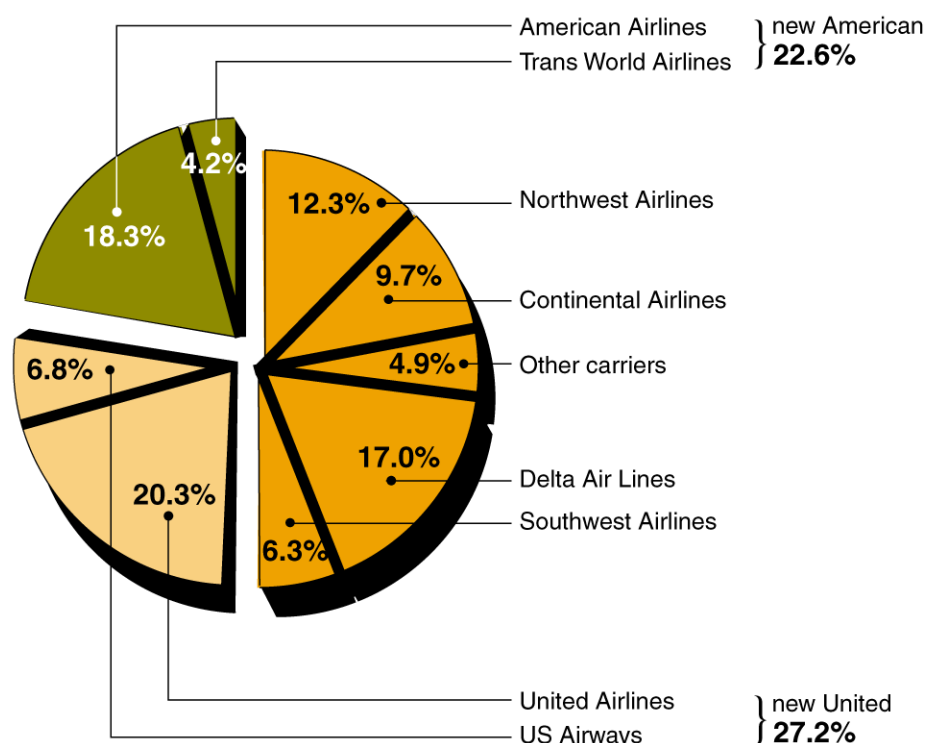
⁷ Justice’s Horizontal Merger Guidelines (United States Department of Justice and Federal Trade Commission Revision to the Horizontal Merger Guidelines (Apr. 8, 1997)) describe the process used to analyze the potential effect of a merger under the Clayton Act. Under the Hart-Scott-Rodino Act, an acquisition of voting securities above a set monetary amount must be reported to Justice for prior review. Justice has the authority to institute judicial proceedings under the Clayton Act if it determines that a merger or acquisition may substantially lessen competition in a relevant market or if it tends to create a monopoly.

Highlights of Potential Changes in Industry Structure

Although the proposed acquisition of TWA by American would not impact as many passengers as the merger between United and US Airways, the transaction itself has the potential for preserving assets in the market. If both the United-US Airways merger and the American-TWA acquisition are consummated, new United would have the largest market share of any U.S. carrier—27.2 percent—and new American would have a 22.6 percent share (based on revenue passenger miles, a recognized measure of airline size⁸). Thus, if both transactions are consummated, new United and new American would together control nearly 50 percent of total airline traffic. Many industry analysts observe that these measures would more than likely not be the end of this move toward further industry consolidation. Figure 1 compares the percentage share of total revenue passenger miles that new American and new United would carry relative to that flown by other major U.S. airlines. Appendix I shows the relative size of major U.S. passenger airlines as indicated by common measures of airline market presence, along with the airlines' 1999 total operating revenue.

⁸ These percentages do not take into account the market share that might be attributable to DC Air or sharing the US Airways Shuttle. Revenue passenger miles represent the number of paying passengers transported over each mile. "Revenue passengers" do not include those who are flying on frequent flyer award tickets and others who did not pay for their flights (e.g., airline employees).

Figure 1: New American and New United Would Have Nearly 50 Percent of Total U.S. Domestic and International Passenger Travel



Note: Percentages may not total due to rounding.

Source: GAO's analysis of data from DOT for the 12 months ending June 30, 2000.

In general, American's acquisition of TWA would lead to the decline of competition in 367 markets—more than the 290 markets in which competition would be reduced from the proposed merger between United and US Airways.⁹ The number of passengers potentially affected by the new American restructuring would be 11 million, compared to 16 million potentially affected by new United. New American would also have a larger increase in the number of markets they could dominate (161) compared to United (126). However, the dominated markets associated with proposed American-TWA arrangement affect fewer passengers than those dominated markets associated with the proposed United-US Airways merger (4.9 million compared to 6.9 million). The total number of markets that new American would dominate would be 552 compared with 1,156 that new United would dominate. On the other hand, new American would

⁹ As we did in our December 2000 report on the proposed United-US Airways merger, we define a market as a city-pair. We define a competitor as an airline that had at least a 10 percent share of the passenger traffic in that market, based on DOT's 1999 data on the top 5,000 city-pair markets, which was the most currently available at the time of our analysis.

increase competition in more markets than new United (150 compared to 65), potentially benefiting more than five times as many passengers (15.4 million compared to 2.9 million).

As a frame of reference for analyzing the competitive significance of the proposed mergers, we compared them with our analysis of the proposal in 1998 by Northwest to acquire a majority of the voting stock in, and enter into an alliance with, Continental.¹⁰ In general, the potential number of markets and passengers who might be adversely affected by either the proposed United-US Airways or American-TWA mergers are much greater than those that might have been affected by the Northwest-Continental stock acquisition and alliance. The number of passengers who could benefit from the American-TWA merger is roughly comparable to those who could have benefited from the Northwest-Continental stock acquisition and alliance. Table 1 summarizes the number of markets and passengers affected by the proposed mergers and compares them to the markets and passengers that potentially would have been affected by the Northwest-Continental stock acquisition and alliance.

¹⁰ Northwest proposed to acquire a majority of the voting stock in, and enter into an alliance with, Continental. Northwest and Continental announced in January 1998 that Northwest was to acquire 8.7 million shares of Continental's stock. These shares gave Northwest 51 percent of the voting rights in Continental. In addition, the two airlines were entering into an alliance that would connect their route systems. A variety of industry analysts told us they believed that Northwest and Continental would not act as independent competitors over the long run. As a result, our analysis of the potential competitive effects of the stock acquisition and alliance assumed that Northwest and Continental would behave as though they had merged. See *Aviation Competition: Effects on Consumers From Domestic Alliances Vary* (GAO/RCED-99-37, Jan. 15, 1999). Our analysis here largely parallels our analysis of the Northwest-Continental stock acquisition and alliance.

DOJ announced a tentative settlement in its antitrust suit opposing Northwest's purchase of a controlling interest in Continental on November 6, 2000. Under the terms of the agreement in principle, Northwest would divest all but 7 percent of the voting interest in Continental and would be subject to significant restrictions on its ability to vote any stock it retains.

Table 1: Comparison of Potential Competitive Impact of the Proposed United-US Airways and American-TWA Mergers with the Proposed Northwest--Continental Stock Acquisition and Alliance

Competitive Factor	American-TWA (1999 data)		United-US Airways (1999 data)		Northwest-Continental (1997 data)	
	Numbers of markets	Passengers affected (millions)	Numbers of markets	Passengers affected (millions)	Numbers of markets	Passengers affected (millions)
Markets where competition would decline	367	11	290	16.0	63	2.0
Newly dominated markets	161	4.9	126	6.9	25	2.4
Total dominated markets	552	27.5	1,156	61.1	492	40.7
Markets where competition would increase	150	15.4	65	2.9	286	15.1

Source: GAO's analysis.

If both mergers proceed, the two new carriers would both compete in 1,106 of the top 5,000 markets. Competition could be reduced in 267 of those markets where, in 1999, about 10.3 million passengers traveled. That is, in 267 markets, as a result of combining what are now separate competitors (i.e., each airline had at least a 10 percent share of the market) through their proposed merger, one competitor would no longer be present. However, the data net out markets where a new effective competitor may be created by the merger (i.e., where the two merging carriers previously had less than 10 percent but combined have over 10 percent.) Table 2 shows the number of markets and passengers that could potentially be affected by a reduction in competition due to the combined effect of the two mergers.

Table 2: Markets Where New American and New United Would Meet and Competition Could be Reduced

Change in the number of competitors	Markets	Passengers (millions)
From 3 to 2	64	2.6
From 4 to 3	123	3.5
From 5 to 3	3	0.1
From 5 to 4	69	3.7
From 6 to 5	8	0.4
Total	267	10.3

Note: Figures may not total due to rounding.

Source: GAO's analysis of data from DOT.

Thus, in 64 of the 267 markets, the two proposed mergers leave new United and new American as the only remaining competitors. In 1999, about 2.6 million passengers traveled in those 64 markets. In 126 markets where 3.6 million passengers traveled in 1999, new United and new American would be two of only three remaining competitors.

Conversely, the proposed United-US Airways and American-TWA mergers would also benefit consumers. In markets where one of the two merging airlines now has limited market shares, the merger would allow them to create competition against other airlines. For example, were both mergers to be approved, approximately 7 million passengers could benefit from gaining an additional competitor in 107 markets. Additionally, by extending the carriers' operations to city pairs where only one of the two airlines previously operated at each endpoint, the merger would create new on-line service between those communities.¹¹ Finally, the merger would benefit members of each airline's frequent flyer programs by expanding the number of destinations that the members could reach. The airlines also assert that the proposed mergers would deliver other benefits as well. For example, American and TWA passengers may benefit through being able to connect to their destination over different hubs.

¹¹ On-line service provides passengers with connecting flight without requiring them to change airlines. Service that requires passengers to change airlines to continue their flights (excluding those requiring a passenger to transfer between a larger airline and its commuter affiliate or other airlines with which it may have a code-sharing agreement) is referred to as "interline" service.

Proposed Arrangements Between American, TWA, United, US Airways, and DC Air Raise Questions and Major Competition Issues

American's acquisition of TWA and its purchase of certain assets of United and US Airways, including a portion of DC Air need to be discussed separately, as the implications would seem to be quite different. Each component of American's proposed transactions raise numerous questions.

-- ***Does American's purchase represent the "least anticompetitive" means to preserve the presence of TWA's assets in the market?*** By many accounts, TWA has been in a difficult financial position for years. Since 1992, TWA has entered bankruptcy three times. It has failed to earn an annual profit during the past 12 years. Regardless of whether TWA would cease operating entirely because of its financial failure, or whether TWA is purchased by another airline, an independent competitive presence in the 103 cities that the airline served will be lost. (However, were TWA to cease operating entirely, the loss of service would likely be temporary, as the would market adjust to meet the demand for travel.)

Whether the loss of competition from TWA is positive or negative depends on a number of factors. DOJ will have to review many of those factors, including increases in market concentration, potential adverse effects on competition of the transaction, possible efficiencies or other benefits, and the likelihood of new entry. It is also DOJ's responsibility to determine whether, for example, absent the merger, TWA's assets would exit the market if it failed, and whether there is no less anticompetitive alternative. On the one hand, we recognize that there are many important considerations involved with preventing TWA from ceasing operations entirely, such as continuing service to markets and maintaining jobs for its employees. On the other hand, the question exists about how the loss of TWA's competitive presence could be mitigated. For purposes of creating more competition in the U.S. domestic aviation market, would it be better if an airline other than American bought TWA?

American's purchase of certain assets of United and US Airways, including a portion of DC Air, raises other significant questions about how competition may be affected. Several issues appear central to an assessment of possible anticompetitive impacts of the proposed transactions:

-- ***How would American's purchasing part of DC Air affect competition?*** As DC Air was originally conceived in the proposed merger between United and US Airways, questions

arose about whether it would be an independent competitor, particularly in certain key markets relative to new United. Now American has proposed to purchase 49 percent of DC Air.

Passengers who may fly on DC Air can now earn American frequent flyer miles instead of miles with United. Passengers, who may be flying beyond Washington, D.C., can now connect with online service onto other American flights rather than on flights operated by United. American's purchase of part of DC Air means that American, not United, would provide some of the aircraft, crew, and other support to DC Air.

-- ***How might American's purchasing part of DC Air affect service to DC Air's markets?*** Under the original proposal to create DC Air, the airline was to serve 44 markets out of Reagan National, most of which are now served by US Airways. DC Air had expressed a commitment to maintain service to essentially all of those cities, using the 222 arrival and departure slots that it would obtain as part of the US Airways divestiture. We do not know what commitment, if any, American expressed regarding maintaining that service. We also do not know what agreements, if any, American made with DC Air to buy out the remaining 51 percent interest in the company or whether American will push to use the slots at Reagan National for other markets.

-- ***How would American's sharing shuttle operations with United alter competition?*** American and United are now proposing to form a joint venture to share the operations of the US Airways shuttle at New York LaGuardia, Boston, and Washington Reagan National for at least 20 years. The two airlines expect to coordinate schedules, ticketing, frequent flyer programs, and access to passenger lounges. We do not yet know how this arrangement might affect price competition in the market.

-- ***Does American's adding flights in certain United-US Airways hub routes enhance competition?*** As part of the agreement with United, American has agreed to provide at least two daily flights on five routes for 10 years. Four of those markets--between Chicago O'Hare and Charlotte, Los Angeles and Philadelphia, San Jose and Philadelphia, and Washington and Pittsburgh--complement American's existing network by originating in one of the airline's "focus cities." However, we do not know what impact the agreement between American and United will have on competition between the two airlines on price and service in those markets.

Critical Public Policy Issues Associated With the Industry's Possible Consolidation

Some industry observers have suggested that the American and United proposals mark the beginning of a new wave of transition. Any industry consolidation that would be brought about by these proposals raises a number of important public policy issues for consideration. We highlight some of these issues—relating to market entry, competition among the newly merged airlines in key markets, potential travel disruption, and small community service—recognizing that there are also many others.

– ***What barriers to market entry might the proposed mergers exert?*** Scores of new airlines have begun commercial passenger service since the deregulation of the industry. Although most failed, other airlines have managed to compete, and some have done so quite profitably. The most notable example, of course, is Southwest. Others—such as ATA, AirTran, and JetBlue—have also experienced success so far. The success of airline deregulation in leading to lower fares and better service stems in part from competition spurred by the entry of new airlines, i.e., low fare carriers are recognized as providing the primary fare discipline in the marketplace. A January 2001 DOT report on exclusionary practices concluded that major airlines have the opportunity and the means to protect their market power by frustrating new entry. DOT found there had been instances in which incumbents drove new entrants out of markets by cutting fares and flooding the market with capacity. Once the new entrant was driven out of the market, the incumbent sought an increase in fares and reductions in service.

If American and United fly nearly half of the industry's traffic, a key issue that policy makers need to address is whether or not new low-cost carriers will be able to enter markets and compete. Because established carriers will control vast numbers of facilities (including slots and gates) at key airports, will those new carriers even be able to offer service in major markets? Will American's and United's sales and marketing efforts (such as their frequent flyer programs and code-sharing affiliations such as the Star Alliance and OneWorld) present barriers that are too great for new entrants to overcome? How effectively will those new carriers be able to compete if the American and United transactions spur additional consolidation in the industry, possibly raising entry barriers even higher?

– ***Would the transactions between American and United alter how they would compete in key markets?*** The proposed United and American arrangements—including the agreements in which American would share the US Airways shuttle with United and compete in

certain markets between United and US Airways hubs– raise questions regarding the extent to which the carriers may compete vigorously. Economic literature and empirical evidence indicate that when there are fewer firms in a market and those firms meet in many markets (e.g., city-pairs), they are likely to recognize their interdependence and compete less vigorously.

To identify the orders of magnitude of markets that might be affected by new United and new American, we examined the number of markets where the merged carriers would each compete.¹² New American would be a competitor in over 2,100 of the top 5,000 markets, while new United would compete in over 2,900. The new carriers would both be competitors in 1,106 markets. Table 3 summarizes the combined passenger shares of the two carriers in these markets.

Table 3: Passenger Shares of New United and New American in Markets Where Carriers Would Both Operate

Combined passenger share of new United and new American	Markets	Percent
81-100%	286	25.9
61-80	324	29.3
41-60	323	29.2
20-40	173	15.6
TOTAL	1,106	100.0

Source: GAO's analysis of 1999 data from DOT.

In 610 of the 1,106 markets (or about 55 percent), the two carriers would account for over 60 percent of the traffic. To the extent the two large carriers recognize their interdependence in these and the other 496 markets where they would both operate, should the carriers not compete vigorously, it could adversely affect fares and service.

– ***Will the public be exposed to greater risk of travel disruptions, in light of the merged carriers' breadth of service?*** Unfortunately, we have witnessed three relatively recent examples of how carrier's labor difficulties can greatly disrupt travel: American's 1997

¹² As noted earlier, in this and in previous reports, we defined a competitor as an airline that carried at least 10 percent of the passenger traffic in a given market. This is the same definition used by DOT.

disruption following its purchase of Reno Air, United's difficulties this past summer, and Delta's current challenges with its pilots. Other labor groups' contracts with the airlines are also coming up for renewal in the near future. If the proposed mergers are approved, and either airline encounters major labor problems, how severely could the public's travel be disrupted? The aviation system has relatively little unused capacity in it now, having been operating at or near record load levels for some time. In general, could the significant integration challenges (not only labor, but also systems and fleets) presented by the American and United proposals make the public more vulnerable to network wide disruptions?

-- ***How might a consolidated industry affect service to small communities?*** The quality of air service to smaller communities and the fares that passengers in those communities pay relative to those paid in larger communities have been issues that the Congress has been concerned about for some time. At the same time, one of the benefits of airline mergers and alliances has been the ability of the larger carrier to provide online service to increased numbers of destinations. For example, the United-US Airways merger could improve competition and service in 256 relatively small markets by providing new online connections. The airlines have also claimed that small communities would gain greater access to international markets through their global alliances. However, the mergers could erode service to many small communities where the merging airlines compete, even if the service provided is over different hubs. One analyst suggested, for example, that American might discontinue TWA's current turboprop service between Bloomington, Illinois, and St. Louis, because American also serves Bloomington, but using small jet aircraft to and from Chicago. Would a more dispersed and competitive market structure offer better promise of providing affordable air access for small and medium sized communities to major US business centers? How might the potential effect of industry consolidation on new entry affect small and medium sized communities?

Conclusions

There are a number of unanswered questions that the Congress, DOJ, and DOT need to address in evaluating the proposed mergers. The proposals by American, TWA, United, US Airways, and DC Air constitute the most significant recent changes that have occurred in the airline industry, and the outcome of these decisions could have both positive and negative effects for consumers for years to come.

This concludes my statement. I would be pleased to answer any questions you or other members of the Committee might have.

Contact and Acknowledgment

For further information on this testimony, please contact JayEtta Hecker at (202) 512-2834. Individuals making key contributions to this testimony included Steve Martin, Chuck Wilson, Triana Bash, David Hooper, and Joseph Kile.

Appendix I

Combined Domestic and International Measures of Airline Size, 12 Months Ending June 30, 2000

Airline	Revenue passenger enplanements ^a		Revenue passenger miles		Total operating revenue	
	Number in thousands	Percent of total	Number in thousands	Percent of total	Dollars in millions	Percent of total
Delta Air Lines	106,218,000	18.8	106,849,814	17.0	14,711	16.3
United Airlines ^a	87,113,000	15.4	127,455,682	20.3	18,027	20.0
American Airlines ^b	85,400,000	15.1	114,832,223	18.3	17,730	19.6
Southwest Airlines ^c	69,056,000	12.2	39,641,182	6.3	4,736	5.2
US Airways ^d	56,417,000	10.0	42,898,817	6.8	8,595	9.5
Northwest Airlines	56,003,000	9.9	77,324,776	12.3	10,276	11.4
Continental Airlines	44,868,000	7.9	60,980,078	9.7	8,639	9.6
Trans World Airlines	26,271,000	4.7	26,650,717	4.2	3,309	3.7
America West Airlines ^e	19,523,000	3.5	18,558,027	3.0	2,211	2.4
Alaska Airlines ^f	13,694,000	2.4	11,962,007	1.9	2,082	2.3
Total ^g	564,563,000	100.0	627,153,323	100.0	90,316	100.0
New United ^h	143,530,000	25.4	170,354,499	27.2	26,622	29.5
New American ^h	111,671,000	19.8	141,482,940	22.6	21,039	23.3

^a“Passenger enplanements” represent the total number of passengers boarding an aircraft. Thus, for example, a passenger that must make a single connection between his or her origin and destination counts as two enplaned passengers because he or she boarded two separate flights.

^aTotal operating revenues are for the parent (UAL Corporation).

^bTotal operating revenues are for the parent (AMR Corporation).

^cSouthwest Airlines provides only domestic service.

^dTotal operating revenues are for the parent (US Airways Group, Inc.).

^eTotal operating revenues are for the parent (America West Holdings, Inc.).

^fTotal operating revenues are for the parent (Alaska Air Group, Inc.).

^gTotals may not add to 100 percent due to rounding.

^hTotals for new United and new American do not make any allowance for those operations that might become part of DC Air or sharing the US Airways Shuttle.

Sources: GAO’s analysis of DOT data.

Related GAO Products

Aviation Competition: Issues Related to the Proposed United Airlines-US Airways Merger (GAO-01-212, Dec. 15, 2000).

Reagan National Airport: Capacity to Handle Additional Flights and Effect on Other Area Airports (GAO/RCED-99-234, Sept. 17, 1999).

Aviation Competition: Effects on Consumers From Domestic Alliances Vary (GAO/RCED-99-37, Jan. 15, 1999).

Aviation Competition: Proposed Domestic Airline Alliances Raise Serious Issues (GAO/T-RCED-98-215, June 4, 1998).

Domestic Aviation: Service Problems and Limited Competition Continue in Some Markets (GAO/T-RCED-98-176, Apr. 23, 1998).

Aviation Competition: International Aviation Alliances and the Influence of Airline Marketing Practices (GAO/T-RCED-98-131, Mar. 19, 1998).

Airline Competition: Barriers to Entry Continue in Some Domestic Markets (GAO/T-RCED-98-112, Mar. 5, 1998).

Domestic Aviation: Barriers Continue to Limit Competition (GAO/T-RCED-98-32, Oct. 28, 1997).

Airline Deregulation: Addressing the Air Service Problems of Some Communities (GAO/T-RCED-97-187, June 25, 1997).

International Aviation: Competition Issues in the U.S.-U.K. Market (GAO/T-RCED-97-103, June 4, 1997).

Domestic Aviation: Barriers to Entry Continue to Limit Benefits of Airline Deregulation (GAO/T-RCED-97-120, May 13, 1997).

Airline Deregulation: Barriers to Entry Continue to Limit Competition in Several Key Domestic Markets (GAO/RCED-97-4, Oct. 18, 1996).

Domestic Aviation: Changes in Airfares, Service, and Safety Since Airline Deregulation (GAO/T-RCED-96-126, Apr. 25, 1996).

Airline Deregulation: Changes in Airfares, Service, and Safety at Small, Medium-Sized, and Large Communities (GAO/RCED-96-79, Apr. 19, 1996).

International Aviation: Airline Alliances Produce Benefits, but Effect on Competition Is Uncertain (GAO/RCED-95-99, Apr. 6, 1995).

Airline Competition: Higher Fares and Less Competition Continue at Concentrated Airports (GAO/RCED-93-171, July 15, 1993).

Computer Reservation Systems: Action Needed to Better Monitor the CRS Industry and Eliminate CRS Biases (GAO/RCED-92-130, Mar. 20, 1992).

Airline Competition: Effects of Airline Market Concentration and Barriers to Entry on Airfares (GAO/RCED-91-101, Apr. 26, 1991).

Airline Competition: Industry Operating and Marketing Practices Limit Market Entry (GAO/RCED-90-147, Aug. 29, 1990).

Airline Competition: Higher Fares and Reduced Competition at Concentrated Airports (GAO/RCED-90-102, July 11, 1990).

Airline Deregulation: Barriers to Competition in the Airline Industry (GAO/T-RCED-89-65, Sept. 20, 1989).

Airline Competition: Fare and Service Changes at St. Louis Since the TWA-Ozark Merger (GAO/RCED-88-217BR, Sept. 21, 1988).

Competition in the Airline Computerized Reservation Systems (GAO/T-RCED-88-62, Sept. 14, 1988).

Airline Competition: Impact of Computerized Reservation Systems (GAO/RCED-86-74, May 9, 1986).

Airline Takeoff and Landing Slots: Department of Transportation's Slot Allocation Rule (GAO/RCED-86-92, Jan. 31, 1986).

Deregulation: Increased Competition Is Making Airlines More Efficient and Responsive to Consumers (GAO/RCED-86-26, Nov. 6, 1985).

(838006)